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No. 89-1023

(2)

In The

Supreme Court of the United States

October Term, 1989

MAYLEE DUBOIS AND VITOUSEK & DICK REALTORS, INC.,

Petitioners,

v.

GERALD HOCKING,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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OPINION BELOW

The opinion of the United States Court of Appeals for the Ninth Circuit sitting en banc is reported at 885 F.2d 1449 (9th Cir. 1989).

STATEMENT OF THE CASE

Introductory Statement

In this brief the respondent, Gerald Hocking ("Hocking" herein), will once again attempt to bring this case back down to earth by addressing the true facts of this particular case and applying those facts to existing law in order to demonstrate why the granting of the petition for writ of certiorari is both unnecessary and inappropriate.

The erroneous innuendos, omissions, and outright misstatements of the facts contained in the petition demand an accurate restatement of the relevant facts of this case, which immediately follows this introductory statement.

The appeal taken by Hocking as plaintiff was from a district court order granting the defendants' motion for summary judgment, in which the district court held that, although it was a close question, the subject transaction did not involve the offer and sale of an "investment contract" and, therefore, a "security" as defined under Section 2 of the Securities Act of 1933, as amended ("the Securities Act" herein), 15 U.S.C. § 77b(1), and Section 3 of the Securities Exchange Act of 1934, as amended ("the Exchange Act" herein), 15 U.S.C. § 78(a)(10). (See the

district court's memorandum decision, which is Appendix D to the petition.)

Since the appellate court is required to review the granting of summary judgment de novo and to view the evidence in the light most favorable to Hocking (as stated in the en banc Ninth Circuit panel opinion on page A-9 of Appendix A to the petition), it is important to note that the only testimonial evidence (in addition to documentary evidence) which is in evidence in this case and a part of the record on appeal is Hocking's affidavit, presented to the district court in opposition to the motion for summary judgment. Accordingly, a copy of that affidavit is included as Appendix I to this brief.

In furtherance of this Court having the true facts before it, a relevant portion of the actual rental pooling agreement which was in effect in this case and the addendum thereto, to both of which documents the petition makes reference without offering them, are also included as Appendix II and Appendix III, respectively, to this brief.

Statement of Facts

In late 1978 or early 1979 Hocking was contacted regarding an investment in Hawaii by petitioner Maylee Dubois ("Dubois" herein), who had been a resident of Nevada but who had become a licensed real estate agent in Hawaii employed by petitioner Vitousek and Dick Realtors, Inc. ("Vitousek and Dick" herein), a licensed real estate broker in Hawaii. Dubois proposed that Hocking purchase a condominium in Honolulu, Hawaii, for investment purposes, and, at the same time, also proposed that he enter into an agreement providing for a

rental pooling arrangement which was connected with the developer and which most if not all of the other condominium purchases in the same building had entered into also. The rental pooling arrangement ("RPA" herein) was part and parcel of the offer to Hocking to purchase the condominium and emphasized the economic benefits to be derived by Hocking from the managerial efforts of third parties designated and arranged for by Dubois from the rental of the condominium and participation in the RPA. Consequently, when Hocking agreed to make the investment, Dubois provided to him various documents for him to sign, including (1) a purchase and sale agreement dated June 23, 1979 to purchase the condominium, (2) a Rental Management Agreement dated July 5, 1979, which was superseded by (3) a so-called Individual Agency Rental Agreement also dated July 5, 1979 (Appendix II hereto), and (4) an Addendum thereto, which was executed by Hocking on July 21, 1979 (Appendix III hereto).

Hocking has emphatically stated that he would never have purchased the condominium without the RPA. (See Appendix I hereto, paragraph 3, page I-2.) He further stated that the RPA was handled by Dubois and the rental agent in Hawaii. (See Appendix I hereto, paragraph 3, page I-2.) Based on the representations of Dubois concerning income to be derived from the RPA, Hocking expected the rental income not only to cover his monthly payment on the purchase price of the condominium but also to provide him with additional income on his investment. (See Appendix I, paragraph 4, page I-2.) Hocking further stated that he knew and relied on the fact that some fifty other condominium owners in the same

building participated in the RPA (see Appendix I, paragraph 6, page I-6) and that, when he visited the condominium, he observed that the building in which it was located was operated like a hotel from the lobby by the RPA company with which Hocking had contracted (see Appendix I, paragraph 6, page I-6). Although all of Hocking's dealings concerning the condominium and the RPA were directly with or through Dubois, Hocking believed that he was purchasing the condominium as a first purchaser from the developer. While he later became aware that he was instead a secondary purchaser and was purchasing the condominium from an original purchaser, Hocking still believed that he was dealing with a RPA company provided by the developer. The linkage between the developer and the RPA company was confirmed when Hocking signed the Addendum to the RPA Agreement on or about July 21, 1979 (Appendix III hereto). After entering into the RPA Hocking relinquished control of the condominium to the RPA company (and had access to it for only two weeks per year). (See Appendix I, paragraph 6, page I-3.)

After losing his entire investment, on December 9, 1983 Hocking filed his complaint in the United States District Court for the District of Nevada against Dubois and her employer Vitousek and Dick. It was on Hocking's third amended complaint filed on February 13, 1985 that Dubois and Vitousek and Dick, on October 31, 1984, filed their joint motion for summary judgment, which was granted by the district court on March 20, 1985 (Appendix D to the petition). Hocking appealed to the United States Court of Appeals for the Ninth Circuit, which issued the original decision of its three-judge panel in *Hocking v. Dubois*, 839 F.2d 560 (9th Cir. 1988), reversing

and remanding the case (Appendix C to the petition). However, after considering a petition for an en banc rehearing of the appeal, on December 7, 1988, the original decision was withdrawn at 863 F.2d 564 (9th Cir. 1989) (Appendix B to the petition). Finally, on September 21, 1989, the en banc panel of the Ninth Circuit issued its decision at 885 F.2d 1449 (9th Cir. 1989), also reversing and remanding the case, from which the subject petition for writ of certiorari was taken.

REASONS FOR DENYING THE WRIT

The *Howey* Test Is Met.

Hocking has met all three requirements of the three-prong test set forth in *SEC v. W. J. Howey Co.*, 328 U.S. 293 (1946). First of all there obviously was an "investment of money." Secondly, the "pooling" aspects of the RPA provides the "common enterprise." And, thirdly, there was, on the part of Hocking, the "expectation of profits from the managerial efforts of others."

The petitioners urge that Hocking had the voluntary decision to do whatever he wanted with the condominium, thereby defeating the third prong of the *Howey* test. However, the facts of the instant case reveal that the realities were otherwise. Hocking could not afford to buy the condominium unless the income from the RPA at least covered his purchase payments, which they did not, so he ultimately lost his entire investment. (See Appendix I hereto.) The statement that Hocking was relying entirely on the appreciation of the value of the condominium for profits to be derived from the investment is entirely

incorrect, based on the facts as presented, which undisputedly the courts, both trial and appellate, are required to view most favorably to Hocking. What was offered to Hocking by the petitioners was that certain "bundle of goods" that gave him what he thought was a good investment which would produce passive income sufficient for him to continue to pay for it. Had it been offered to him otherwise, he would not have made the investment. (See Appendix I hereto.)

His anticipated (and misrepresented) profits were clearly to have been derived from the efforts of others. He had no real choice. The building in which the condominium was located was being run like a hotel by the same company with which Hocking and the other condominium owners had contracted their RPA. The economic realities were that Hocking either went along with the arrangement or he couldn't (and shouldn't) accept the investment offer made to him by Dubois. (See Appendix I hereto.)

The petitioners' contention, on page 20 of their petition, that "Hocking could terminate both the Rental Management Agreement and the Pooling Agreement on extremely short notice, and as such he could regain total control and unimpeded access to and use of his condominium," is erroneous and misleading. As stated above the so-called Rental Management Agreement was superseded by the so-called Pooling Agreement, so the former's termination provisions were also superseded by the latter and are irrelevant and inapplicable. The so-called Pooling Agreement, however, had no such short termination provision but could only be terminated on ninety days' notice prior to the anniversary date. After

the expiration of the first year of the term of the RPA agreement, Hocking had virtually no control over the condominium. (See Appendix II.)

The petitioners also argue that the purchase of the condominium and the entry into the RPA agreement were totally separate transactions and that there was no affiliation or linkage between them. This argument flies in the face of the facts presented by Hocking that the offer to him to purchase the condominium was tied to the RPA agreement, without which he would not have made the investment. (See Appendix I hereto.) Furthermore, the Addendum to the RPA agreement (Appendix III hereto) also supports Hocking's position by extending the time for the RPA agreement to take effect. The Addendum also supports Hocking's contention that he thought that he was purchasing directly from the developer, because the Addendum shows that the developer needed additional time to complete the building and all of the condominiums contained therein including the one purchased by Hocking.

The only other argument that could supply a reason for the Addendum is a nefarious one, namely that the developer and the RPA operator, obviously affiliated and linked together by mutual interest, if nothing else, wanted to provide an artificial space of time from which they could argue that their joint transactions did not involve the offer and sale of securities. However, in this case, as has been stated and restated herein, the facts presented must be viewed most favorably to Hocking. Accordingly, whichever argument may be accepted still leads to the same conclusion that the transactions in the case involved the offer and sale of a security.

The facts in this case offer no major departure from existing law under *Howey* and its progeny. Moreover, the en banc panel of the Ninth Circuit retreated from the "bright line rule" enunciated in the three-judge panel's decision and refused to state unequivocally that the "bundle of goods" offered and sold in this case was a security; rather, the majority held only that there were sufficient facts presented here where the district court could find that there was a security, not that the district court was required to do so after hearing the facts from both sides. Obviously, therefore, since this case has not yet been tried, consideration of it at this stage by the Supreme Court of the United States is premature.

The Ninth Circuit's Reasoning Is Sound.

Even if the majority decision of the Ninth Circuit en banc panel is viewed as expansive of *Howey* and the other cases decided under it in the various circuits and elsewhere, as contended, nevertheless, and for all of the good reasons stated above, the present reasoning of the Ninth Circuit on this issue is sound.

To differentiate between the sale of a condominium offered with an RPA when it is offered by the original developer rather than by a subsequent owner or by a broker has no sound reason. Neither does it make good sense to differentiate between the situation where the offerors and sellers of the condominium and the RPA are different and separate entities rather than the same one. To make such differentiations is the essence of "form over substance," which is precisely what the enactment of the securities laws, their regulation by the Securities and

Exchange Commission, and their interpretation by the Courts have sought to avoid. It is urged upon this Court that this is also precisely what the Ninth Circuit has done in the instant case, and its decision should be left undisturbed.

There Is No New Burden on the Real Estate Industry.

To characterize as an overstatement the position that the Ninth Circuit decision in the instant case creates a new burden on the real estate industry is itself an understatement.

The real estate industry, including both developers and brokers, have been on notice since 1973, when the Securities and Exchange Commission issued Securities Act Release No. 33-5347, 17 C.F.R. 231, 38 Fed. Reg. 1735, 1 Fed.Sec.L.Rep. (CCH) ¶ 1049 (Jan. 4, 1973), that it was necessary to be very careful with offering and selling real estate condominiums with rental pooling arrangements. The subject Ninth Circuit decision, which the petitioners seek to overturn, merely gives additional guidelines for real estate brokers to follow in order to prevent liability under the federal securities laws, which should be a help and not a hindrance to them.

To suggest that offers and sales which fit into the present Ninth Circuit guidelines will all have to be registered under the Securities Act is ludicrous. The petitioners and particularly their counsel of record well know that there are exemptions from registration of which advantage could be taken, involving relatively little cost in comparison to full registration costs. If the package which is being offered is a security, then it should be offered as

such, and, if it has to be sent by the real estate broker down the street to the neighborhood securities broker-dealer, then that is what the law requires, because, if the package is truly a security, then the prospective offeree-purchaser is entitled to the protection which the securities laws are supposed to provide.

CONCLUSION

The Ninth Circuit decision which the subject petition seeks to overturn is entirely consistent with *Howey* and its progeny and, in any event, is based on sound reasoning because, upon careful examination, it makes good sense and, therefore, good law. Moreover, the decision is only one which says that the district court erred in finding that the facts of this case could not involve the offer and sale of a security – not that there absolutely is a security present here. This case should now be considered by the district court under the standards enunciated by the Circuit Court; consequently, it is premature for the Supreme Court of the United States to hear this case at this time. Finally, the Ninth Circuit has put no new burden on the real estate industry by its scholarly decision. Accordingly, the petition for writ of certiorari should be denied.

Respectfully submitted,

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Counsel of Record for Respondent

APPENDIX I

AFFIDAVIT OF GERALD M. HOCKING

STATE OF NEVADA)
) SS.
COUNTY OF CLARK)

I, GERALD M. HOCKING, being first duly sworn upon my oath, depose and state as follows:

1. I am the plaintiff in the above-captioned case, and I make this affidavit on my personal knowledge in opposition to Defendants [sic] Joint Motion for Summary Judgment.

2. When my deposition was taken on July 28, 1984, I had not reviewed the various documents which I have accumulated in connection with the above-captioned case. However, I have recently done so thoroughly. Thereafter, I also reread the transcript of my said deposition. The questions and answers therefrom quoted by the defendants in their so-called Statement of Material Facts in support of their motion for summary judgment are incomplete: in certain instances the obvious next question was not asked; I was not given the opportunity to explain my answers; and my attorney, in his discretion, did not choose to cross-examine me to provide additional information or such explanations.

3. When I testified in my deposition that I did not depend upon the company that provided the pooling arrangement to increase the value of the condominium, I only meant that I thought that the pooling arrangement

in and of itself would not affect the value of the condominium at resale. Whether the statement is in fact true I do not know. The fact is that I would never have entered into the transaction without the pooling arrangement, and I so testified in my deposition on page 62, lines 24-25, and page 63, lines 1-5:

> "There's one simple fact. Your question is could I have bought the place without a rental agreement. That is the question, but that question isn't complete in that would I have.
>
> "No I would not have. Could I have, yes, but as I bought it, it was understood to be handled by my agent and the company in Hawaii."

4. Similarly, I also testified that defendant Maylee DuBois did not make any representations as to how much rent I would expect to receive on a monthly basis. Again, it is accurate that she did not state a specific figure to me. However, as I also testified, she did tell me what I could expect on a daily basis and I so testified on page 27, lines 13-15:

> "As I remember, I was informed that those condominiums were renting anywhere from $80 to $100 to $110, average $100 a day."

It was simple arithmetic for me to calculate that the monthly income, based on the daily rental figures represented to me, would be $2,000-$3,000 per month. Again, while I did not expect my rental income from the pooling arrangement to increase the resale value of the condominium, I certainly did rely upon the expected rental income not only to cover the monthly payment on the purchase price but also to provide me with additional income.

5. The critical fact is – and I was never asked this question at my deposition – that the failure to receive the expected rental income which was represented to me resulted in the loss of my investment in the condominium. The reason is obvious: I had expected the rental income represented to me to at least cover my monthly payment, which it did not; even though it was represented to me that the resale value of the condominium was increasing, I finally discovered that it was not; and I could not afford to put any more money into the condominium. Specifically, defendant Maylee DuBois consistently told me throughout the period of my ownership of the condominium that it was appreciating in value; however, when I realized that I was not going to derive rental income, I listed the condominium for sale with defendant Maylee DuBois at the price she advised, namely $190,000, and I later found out both that the listing had never been effected and that the price was entirely too high.

6. I knew and relied upon the fact that approximately fifty other condominium owners participated in the pooling arrangement of which I was a part. The monthly statements which I received from the company operating the pooling arrangement indicated that I was receiving approximately 2% of the total rental income from the building each month. When I visited my condominium, I observed that the building in which it was located was operated like a hotel from the lobby, and I received copies of the brochures and advertisements which the pooling company distributed to the mainland. I relinquished control of the condominium to the pooling company right at the time I purchased it and only had access to it for not more than two weeks per year.

7. The contention by the defendants that I am a "sophisticated investor" is ridiculous. As I testified in my deposition, I am a high school graduate and have only the equivalent of one year of college. I have never taken any courses or had any special training whatsoever in investments or real estate or anything else for that matter. I knew nothing about tax free exchanges, and the proposal for the tax free exchange referred to by the defendants was one that was entirely laid out for me by a local real estate agent in Las Vegas, Nevada. I believe that the best evidence of my lack of sophistication is the fact that I accepted for such a substantial period of time the fraudulent misrepresentations of Maylee DuBois. The contracts that were presented to me by defendant Maylee DuBois and which I signed were represented to me to be standard forms that I neither read nor fully understood. In particular, the pooling agreements were printed forms, the terms and conditions of which I was given no opportunity to discuss or negotiate.

8. Defendants further contend that I have admitted that I could have sold the condominium for $135,000 and realized a profit from the purchase price of $115,000 at one point in time before the market price went down. Actually, my testimony in my deposition was as follows, on page 48, lines 4-9:

> "I remember her [defendant Maylee DuBois] telling me that it was a very good buy and at one time or another during the signing and such she had informed me it had already gone to $135,000 and holding onto it for a short time, keeping it rented out, and turning it around, I should realize a very nice profit from it."

I have absolutely no reason to believe that defendant Maylee DuBois' representation of the $135,000 figure at that time was accurate (any more than the inaccurate $190,000 figure that she related to me). Furthermore, she emphasized continuously that the value was steadily increasing and that I should not sell the condominium. I was only when I could not longer afford to put more money into the condominium that she agreed to list it (which she did not do), at which time she set the price of $190,000, knowing full well that the condominium could not be sold for what I had in it, let alone at a profit.

/s/ Gerald M. Hocking
GERALD M. HOCKING

SUBSCRIBED and SWORN to before me this 16 day of November, 1984.

/s/ S. Miller
S. MILLER

[SEAL]
Notary Public-State of Nevada
CLARK COUNTY
My Appointment Expires Jan. 17, 1987

APPENDIX II

2121 ALA WAI
INDIVIDUAL AGENCY RENTAL AGREEMENT
FOR POOLED OPERATION

THIS AGENCY RENTAL AGREEMENT is entered into this 5th day of July 1979, by and between Gerald M. Hocking (hereinafter referred to whether one or more persons or entities as "Owner"), and HOTEL CORPORATION OF THE PACIFIC, INC., a Hawaii corporation whose executive offices are located at 2299 Kuhio Avenue, Honolulu, Hawaii 96815 (hereinafter referred to as "Agent"). In consideration of the respective covenants and agreements herein contained, Owner and Agent herein agree as follows:

* * *

2. TERM

This Agreement shall become effective ___, 19 ___, and shall continue in full force and effect until MIDNIGHT, DECEMBER 31, 1984. Either party may elect to terminate this Agreement by giving written notice to the other party ninety (90) days prior to an anniversary date of this Agreement except that during the initial year Owner may elect to terminate at any time by giving written notice to Agent fifteen (15) days prior to date of intended termination. For the purpose of this Agreement an "anniversay date" shall be deemed to be JANUARY 1st. In the event this contract is terminated as provided herein, or the Unit sold during the term of this Agreement, Owner agrees that such termination or sale shall be subject to all confirmed rentals therefore arranged by

Agent and Owner agrees to advise Buyer of this Agreement during escrow. Agent, at his sole option, is hereby provided two (2) successive five (5) year extensions of this Agreement which may be exercised by Agent giving written notice to Owner six (6) months prior to the Agreement's then expiration date.

This Agreement will terminate if 75% of Owners then participating in Agent's program at Property elect (one vote per unit) to do so and that the Rental Advisory Committee provide to Agent written notice to such election one hundred twenty (120) days in advance of date of intended termination. Agent shall have the right to terminate after six (6) months from the inception of Agent's program at Property, should the number of units participating in Agent's program fall below 40% of all units in Property.

* * *

IN WITNESS WHEREOF, the parties hereto have executed this Agreement the day and year first above written.

Executed the Date above written:

By /s/ [Illegible]
HOTEL CORPORATION
OF THE PACIFIC

By /s/ Gerald M. Hocking
OWNER

By_____
OWNER

APPENDIX III

ADDENDUM TO 2121 ALA WAI INDIVIDUAL RENTAL AGENCY AGREEMENT FOR POOLED OPERATION

Consistent with the Developer of 2121 Ala Wai's original sales covenants, particularly Paragraph 23 of the Developer's Sales Agreement, Owner and Agent agree to waive all aspects of this Agreement with respect to pooling or sharing of expenses with other units in Property until which time the Developer has closed the sale of all units in the Property or until December 31, 1982, whichever shall occur first.

During such interim period Owner shall have no claim to any income from the rental of any unit other than his own; nor shall any other unit owner have any claim to any income from the rental of Owner's Unit. Agent shall distribute to Owner the net income of the Unit for the preceding calendar month together with the monthly operating statement. The monthly net income of the Unit shall be determined by deducting from the gross receipts of the Unit, the Agent's fees, any applicable travel agent's fee, and an amount, initially set at 25% of the gross income, which is estimated to be sufficient to cover all operating expenses and such reasonable sums as the Agent may reasonably deem necessary or appropriate to retain as reserves to meet abligations [sic] which will or may become due thereafter, taking into account estimated future income. As operating experience is gained, this 25% figure will be adjusted upwards or downwards by the Agent to insure that there will be no deficit or unreasonable surplus.

IN WITNESS WHEREOF, the parties hereto have executed this Addendum.

By /s/ [Illegible]
HOTEL CORPORATION
OR [sic] THE PAFCIFIC

date 7/31/79

By /s/ Gerald M. Hocking
OWNER

By /s/ Unit 2603
OWNER

date 7/21/79